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From:

Sent: Wednesday, November 10, 2010 9:24:33 AM

To:

Cc:

Subject: RE: IRC 988 Issue/Reverse SILO

You have asked for my views regarding a foreign currency loss claimed by the taxpayer. The subject of the claimed loss was a promissory note given by _____, to _____ in _____. In _____, the note was exchanged for two promissory notes denominated not in _____, as was the original note, but in _____. Whether the loss purportedly resulting from this exchange should be allowed depends on whether the _____ promissory note represented genuine debt for federal income tax purposes.

One argument for not respecting the debt is that in substance there was no consideration for the promissory note. According to your draft Notice of Proposed Adjustment, the purported consideration was _____ acquisition of a _____ facility from _____ and _____ agreement to pay the purchase price. In substance, however, _____ did not own the facility and could not sell it to _____. _____ had acquired bare legal title to the facility in a transaction the taxpayer would concede was a financing, not a sale, and which can more fairly be described as a sale of tax benefits to _____. Moreover, _____, in substance, would never pay _____ any sum of money that can be characterized as the purchase price of the facility. This amount, rather, would be "paid" from an account that was established as part of the _____ transaction and at all times was within the control of _____ and unavailable to _____ or any other taxpayer-related entity. (As you point out, under this view of the transaction, taxpayer should not recognize foreign currency gain on any disposition of the foreign currency in the account, as it would not be treated as the account's owner.) Besides the apparent lack of consideration for the _____ promissory note, the infrequent and irregular payment of interest also is a factor supporting disregard of the debt for federal income tax purposes.

On the other hand, taxpayer may have arguments for respecting the _____ promissory note, including theories that do not rely on the purported consideration provided to _____. _____